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FM AMEMBASSY BUENOS AIRES  
TO RUEHMN/AMEMBASSY MONTEVIDEO IMMEDIATE 5964  
RUEHC/SECSTATE WASHDC IMMEDIATE 6606  
INFO RUEHBR/AMEMBASSY BRASILIA 5606  
RUEHSO/AMCONSUL SAO PAULO 3047

UNCLAS BUENOS AIRES 002636

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MONTEVIDEO PLEASE PASS TO CODEL GOODLATTE

E.O. 12958: N/A

TAGS: [PGOV](#) [PREL](#) [ECON](#) [PARM](#) [SNAR](#) [AR](#)

SUBJECT: ARGENTINA SCENE-SETTER FOR CODEL GOODLATTE

11. INTRODUCTION AND SUMMARY: On behalf of Embassy Buenos Aires, I warmly welcome your visit to Argentina November 29-December 3. As one of the world's major agricultural producers and exporters, Argentina's policies in this sector have an important impact on U.S. agriculture. You will have the opportunity during your meetings to encourage your Argentine interlocutors to develop and implement a sound and long-term agricultural policy based on the principles of open and competitive markets. You can also encourage GOA officials and congressional leaders to take a more active and constructive approach to the Doha Round trade negotiations. During your visit, you will hear from U.S. companies doing business in Argentina, including Monsanto and Cargill, and some of the problems and challenges they face.

12. Your visit comes at a time of considerable ferment in the Argentine political and economic arenas. In October 2005 President Kirchner won a resounding victory in mid-term legislative elections. Based on these results, Kirchner has further tightened his already firm control of political and economic policy. Political interest is focusing increasingly on next year's presidential elections. The agricultural and livestock sectors, two of the mainstays of the Argentine economy (over 50 percent of total Argentine exports are represented by agricultural, livestock, and food shipments), have been a focus of GOA policies to maintain low domestic prices and increase government revenues. These GoA policies, which include a menu of export tariffs, export quantity controls and explicit and implicit price controls have been criticized by agricultural and livestock players. Nevertheless, Argentina has sustained an impressive economic recovery since suffering the worst economic crisis in its history ) including the largest sovereign default in history and a devaluation of its currency ) in 2001-02. Its agricultural export-led boom has triggered three consecutive years of 9 percent real GDP growth beginning in 2003. END INTRODUCTION AND SUMMARY.

Background

13. Argentina was once one of the richest countries of the hemisphere, achieving a GNP per capita that was among the highest in the world in the early 20th century. However, the history of Argentina over the last 70 years has been one of economic decline and political instability. Many Argentines are at a loss to explain how their country, blessed with rich natural resources, a fertile land and manageable population numbers, could have fallen so far. Some blame the military dictatorships, which predominated between 1930-1983; others blame Peron and "Peronism;" and a significant number blame external factors: the IMF, the U.S., and, to a lesser extent, Europe, especially following the 2001-2002 economic crisis,

the worst in Argentine history. The election of left of center Peronist Nestor Kirchner in 2003 marked a significant shift in Argentine foreign policy, aligning the country more closely with its MERCOSUR partners and less closely to the U.S. That said, Kirchner has cooperated closely with the U.S. on a number of issues, including counter-terrorism and narcotics, and regional problems like Bolivia and Haiti.

#### Political Landscape

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¶4. Kirchner is widely perceived to be the strongest Argentine President since the return to democracy in 1983, and he faces a weak and divided opposition. Argentines give Kirchner much of the credit for the country's Phoenix-like recovery from its 2001-2002 economic crisis, an event equivalent to our Great Depression. Political interest is focusing increasingly on next year's presidential elections. It is widely thought that, if he chooses to run, Kirchner will win reelection easily. There has been some speculation, including from the president himself, that he will not be a candidate and that his wife, Senator Cristina Fernandez de Kirchner, will stand in his place. Potential opposition candidates include former Finance Minister Roberto Lavagna, businessman and president of the Boca Juniors soccer team Mauricio Macri, and the counter-left national congresswoman Elisa Carrio.

¶5. Argentina has played a positive role in promoting human rights and democratic institutions in the hemisphere, particularly in Haiti and Bolivia. Along with a number of its neighbors, Argentina currently has 575 peacekeeping troops in Haiti in support of MINUSTAH, reflecting its traditionally strong support of UN peacekeeping operations and commitment to Haiti.

¶6. Kirchner's administration has strongly supported counter-terrorism policies, having been a victim itself twice in the early 1990's of international terrorist attacks. The GOA has ratified all of the 12 international counter-terrorism conventions. Argentina is a participant in the Three Plus One regional mechanism, which focuses on possible terrorist-related activity in the Tri-border region between Argentina, Brazil, and Paraguay.

¶7. The GOA has been a strong international voice on arms control and nonproliferation issues. On Iran, the GOA voted to refer Iran's noncompliance to the UNSC at the September 24 IAEA Board of Governors meeting. The GOA has also endorsed the Proliferation Security Initiative (PSI).

#### Agriculture

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¶8. The agricultural and livestock sectors, two of the mainstays of the Argentine economy (e.g., over 50 percent of total Argentine exports are represented by agricultural, livestock, and food shipments), have been negatively affected by GOA's policies to contain inflation. This targeting is due to the fact that food items carry major weights in the determination of the Consumer Price Index (CPI). The two principal policy initiatives which the GOA has chosen to curb inflation have been through price and export controls. The chief agricultural and livestock products that have been affected by this policy are grains (wheat and corn), dairy, and meat. The GOA has watched, with great concern, as the international price of wheat has sharply increased, due to a major drought in Australia, and lower than expected production in the U.S. and Argentina. Argentine exporters, taking advantage of strong international prices, have rapidly registered export sales to the point where residual supplies for domestic consumption, especially for the milling industry, have become extremely tight. Argentina is the number 5 exporter of wheat in the world. In an attempt to maintain the price of bread at what it considers a reasonable level, the GOA recently has mandated Argentine exporters to sell 4 million tons of wheat to the milling industry at a price (US\$120 per ton), well below the

international price.

¶9. Corn prices have also caught the attention of the GOA. What with uncertainty in the U.S. over availability of supplies for ethanol and food and feed stocks, which has boosted prices, Argentine corn exporters (Argentina is the number 2 exporter of corn in the world) have registered export sales at a record pace (10.5 million tons have been registered on next year's corn crop, estimated around 17.6-18 million tons), taking advantage of favorable external conditions. The GOA has reacted by freezing further registrations, hoping to ensure sufficient corn for domestic use (the corn is used, in the main, as feed for livestock and poultry, and for food) without putting upward pressure on prices. Earlier this year, as prices of dairy products rose, the GOA reacted by increasing export taxes on cheese and powdered milk. These taxes undercut previously strong growth by this industry, and have led one of the main dairy enterprises, which was suffering from heavy indebtedness and low profitability, to seek to merge with ADECOAGRO, a U.S. investment group led by George Soros.

¶10. Since Argentina has the highest per capita beef consumption in the world (about 63 kilograms per capita), the GOA has been extremely concerned about the price of this commodity. Late last year, in the face of rising domestic prices, the GOA increased the export tax on fresh beef from 5 to 15 percent, and the minimum slaughter weight to 280 kilograms. In March, it banned almost all fresh beef exports (except those destined to fulfill the European Union's Hilton Quota, and those involved in country-to-country agreements). The GOA hoped that a ban on beef exports would translate into increased domestic supply, which would put downward pressure on ascending domestic prices, fueled by the economic recovery, and the shortage of beef in international markets due to food-and-mouth disease outbreaks in Brazil. Over the last five months, the GOA has relaxed some of these restrictions, after it realized that market intervention had become counterproductive. It is, however, again poised to intervene aggressively if it believes that beef prices are increasing at an unreasonable rate.

#### Economic Situation

¶11. Argentina has had an impressive economic recovery since suffering the worst economic crisis in its history -- including the largest sovereign default in history and a devaluation of its currency -- in 2001-02. An export-led boom triggered three consecutive years of 8.8-9.2% real GDP growth beginning in 2003, with GDP reaching \$182 billion in 2005, approximately \$4,700 per capita. The Kirchner Administration has ably managed the nation's public finances and achieved large budget surpluses. Industrial and construction activity are growing rapidly, and tourism has boomed, with a record high of an estimated 3.7 million foreign tourists visiting in 2005. Economic expansion is creating jobs and unemployment dropped from 20.4% in the first quarter of 2003 to 10.2% in the third quarter of 2006. Investment in real terms jumped 22.7% in 2005. Poverty has also fallen from the post-crisis level of 60 percent, but remains stubbornly high. During the first half of 2006, 31% of the population was living below the poverty line. Argentina negotiated a debt exchange with 76% of its creditors in 2005 (paying 30 cents on the dollar), and paid off its nearly \$10 billion debt to the IMF on January 3, 2006.

¶12. Argentina's impressive recovery, which has led to improvements in key socio-economic indicators, can be attributed to a number of factors. First, following a decade of market reforms, the economy was fundamentally sound except for the high level of indebtedness. Second, the adoption of a market-based exchange rate regime in early 2002 and the combination of high commodity prices and low interest rates catalyzed Argentina's export-led boom. Exports are at record levels and Argentina's trade surplus totaled \$11.3 billion in 2005. Foreign trade equaled approximately 38% of GDP in 2005 (up from only 11% in 1990) and plays an increasingly important role in Argentina's economic

development. The government has maintained a primary fiscal surplus and continues to accumulate reserves, which exceeded \$30 billion in October 2006. Argentina should continue to perform well in 2007 with GDP growth projected at 7% and inflation in the 7-10% range. Nevertheless, slowness in addressing public service contract renegotiations, capacity constraints, potential energy shortages in the face of high growth and distorted energy prices, inflation and the government's heterodox policies to contain it (including pressure on the private sector to maintain price controls), and a still-weak investment climate are potential obstacles to sustaining the recovery.

¶13. U.S. agribusiness companies have invested heavily in the Argentine economy for many decades, and have made major contributions to the agricultural and livestock sectors. You will be meeting with representatives of a number of these enterprises at an American Chamber of Commerce breakfast and will be hosted to lunches by two: Cargill and Monsanto. Cargill is making investments valued at \$330 million in agricultural processing facilities (soybeans, malt), a packing house, and port facilities. Over the last two years, business and profitability in this sector have been challenged by GOA intervention exemplified by the ban on exports of fresh meat, price controls imposed on wheat, and the freezing of export sales of corn. Monsanto faces major challenges, in particular its inability to collect royalties on the Round-Up Ready soybean technology, which has revolutionized soybean production in Argentina. It has attempted to negotiate a solution to this issue with seed companies, farm organizations, and other stakeholders and launched court cases in Europe. Unfortunately, Monsanto and GOA authorities have not found a meeting of the minds to solve this important issue of intellectual property rights protection.

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